

**Performance Audit  
Review of the 1999 TIF Annual Report**

August 2000

**City Auditor's Office**

**City of Kansas City, Missouri**



August 16, 2000

Honorable Mayor and Members of the City Council:

The City Council Finance and Audit Committee directed the City Auditor's Office to review *The Tax Increment Financing 1999 Annual Report*. This audit report addresses the following questions:

- What information does the 1999 annual report provide?
- What other information about tax increment financing (TIF) should be provided to City Council?

*The Tax Increment Financing 1999 Annual Report* includes information on the 37 individual TIF plans in Kansas City. The annual report also includes information from a survey of the developers of most of the plans. The annual report does not include a copy of each redevelopment plan, which is one of the requirements of state statute. Although including each plan is not practical, the report should explain how readers could obtain a copies of redevelopment plans.

In addition to the annual report, decision-makers need information to examine the use of incentives in a broader context. Like major capital expenditures, development incentives should be considered in the context of the city's overall financial condition. The Finance Department should report aggregate measures to relate development incentives to the city's financial condition. The report should include measures of revenues and expenditures, debt, and associated tax base.

The Finance Department should issue an annual report of financial information about TIF and other economic development incentives to the City Plan Commission and City Council. Such a report would enable the City Council, city management, and citizens of Kansas City to examine the use of incentives in the broader context of their impact on the city's overall fiscal condition by offering aggregate data on revenues, expenditures, debt levels, and associated portions of the tax base. The report would offer policymakers greater insight into the fiscal implications of incentive use and would serve as a reference when new TIF projects are being evaluated.

The draft performance audit report was sent to the city manager and the executive director of the TIF Commission on June 12, 2000. Their written responses are included as appendices. We appreciate the courtesy and cooperation extended to us during this project by Economic Development Corporation and city staff. The audit team for this project was Bill Davis, Michael Eglinski, and Robin K. Reed.

Mark Funkhouser  
City Auditor



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# Performance Audit: Review of the 1999 TIF Annual Report

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## Introduction

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## Audit Objectives

The Finance and Audit Committee directed the City Auditor's Office to review the *Tax Increment Financing 1999 Annual Report*.<sup>1</sup> The review was conducted pursuant to Article II, Section 13 of the Charter of Kansas City, Missouri, which establishes the Office of the City Auditor and outlines the city auditor's primary duties.

A performance audit is an objective, systematic examination of evidence to independently assess the performance of a government organization, program, activity, or function in order to provide information to improve public accountability and facilitate decision-making.<sup>2</sup> This audit was designed to answer the following questions:

- What information does the 1999 annual report provide?
- What other information about tax increment financing should be provided to City Council?

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## Scope and Methodology

The audit was designed to address concerns raised in prior audits and reports regarding the information that the mayor, city manager and City Council receive about tax increment financing (TIF) and the context in which that information is conveyed. This audit was not designed or intended to review the accuracy of data included in the *Tax Increment Financing 1999 Annual Report*, nor the TIF Commission's Annual Financial Statements. The audit did not attempt to measure progress on the implementation of recommendations in the City Auditor's Office's September 1998 report entitled *Performance Audit of Tax Increment Financing*.

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<sup>1</sup> *Tax Increment Financing 1999 Annual Report, Volume I: Plan Summary and Results and Volume II: State of Missouri Annual Report*, Economic Development Corporation of Kansas City, Missouri, October 13, 1999.

<sup>2</sup> Comptroller General of the United States, *Government Auditing Standards* (Washington, DC: U.S. Government Printing Office, 1994), p. 14.

We conducted this audit in accordance with generally accepted government auditing standards, with the exception of the completion of an external quality control review of the City Auditor's Office within the last three years.<sup>3</sup>

Our methods included:

- Reviewing the *Tax Increment Financing 1999 Annual Report*.
- Interviewing staff of the Economic Development Corporation (EDC) and TIF Commission.
- Reviewing city code and state statutes.
- Interviewing city staff and selected elected officials for their views on available information about TIF.
- Reviewing past audits and reports issued by the City Auditor's Office.

No information was omitted from this report because it was deemed privileged or confidential.

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## **Background**

Tax increment financing (TIF) is one of several economic incentive programs offered by the city to encourage development and redevelopment. It is intended to reduce or eliminate adverse conditions in an area and to enhance the tax base. Other incentive programs include Land Clearance for Redevelopment Authority, Chapter 353 tax abatement, and Chapter 100 bonds.

TIF is a development incentive to eliminate blight and to fund redevelopment that otherwise would not occur. TIF is based on the premise that redevelopment will result in an increase in the value of real property and other economic activity that will generate new tax revenue to the municipality. The new or increased local tax revenues resulting from TIF redevelopment projects are called "tax increments." The tax increment from local real property taxes (PILOTS) and 50 percent of the increment from economic activity taxes (EATS) are available to finance eligible project costs, such as the construction of public infrastructure, site clearance, and related project expenses.<sup>4</sup>

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<sup>3</sup> The last review was in April 1995. A peer review is planned for the current year.

<sup>4</sup> *Economic Development Incentives*, City Planning and Development Department, Finance Department, and Economic Development Corporation, August 1999, p. 1.



### **State Statute Requires an Annual Report**

Missouri statute requires an annual report by the governing body of a municipality or its designee on the status of each redevelopment plan and project.<sup>5</sup> The TIF Commission, acting as the city's designee, files the report with the Missouri Department of Economic Development.

### **City Council May Require Additional Information**

In addition to several specific items of information, Missouri statute requires TIF annual reports to include “any additional information the municipality deems necessary.”<sup>6</sup> This provision enables City Council to require any other information from the TIF Commission on individual TIF projects or the program as a whole to be included in the annual report. The City Charter also authorizes City Council to request any information relating to city affairs or matters of municipal interest. These provisions may be applied to obtain specific or aggregate information relevant to enable City Council to set overall policy or monitor the results of their decision-making on TIF-related matters. To date, the City Council has not enacted an ordinance or resolution to call for any additional information.

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<sup>5</sup> RSMo 99.865.

<sup>6</sup> RSMo 99.865.



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## Findings and Recommendations

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### Summary

The *Tax increment Financing 1999 Annual Report* includes information on the 37 individual TIF plans in Kansas City. The annual report also includes information from a survey of the developers of most of the plans. The annual report does not include a copy of each redevelopment plan, which is one of the requirements of state statute. Although including each plan is not practical, the report should explain how readers could obtain a copies of redevelopment plans.

In addition to the annual report, decision-makers need information to examine the use of incentives in a broader context. Like major capital expenditures, development incentives should be considered in the context of the city's overall financial condition. The Finance Department should report aggregate measures to relate development incentives to the city's financial condition. The report should include measures of revenues and expenditures, debt, and associated tax base.

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### Annual Report Provides Information on Individual TIF Plans

The *Tax Increment Financing 1999 Annual Report* includes information on the 37 individual TIF plans in Kansas City. State law requires annual reporting on individual TIF plans; the report responds to these statutory requirements. The report also includes some information provided by developers about the TIF plans.

#### State Requires Information on Each TIF Plan

Volume II of the annual report includes information on each of the 37 TIF plans in a format established by the Missouri Department of Economic Development. The following information is required by state statute and is in the annual report:

- Amount and source of revenue in the special allocation fund;
- Amount and purpose of expenditures from the special allocation fund;

- Amount of any pledge of revenues, including principal and interest on any outstanding bonded indebtedness;
- Original assessed value of the redevelopment project;
- Assessed valuation added to the redevelopment project;
- Payments made in lieu of taxes received and expended;
- Economic activity taxes (EATs) generated within the redevelopment area in the year prior to approval of the plan;
- EATs generated within the redevelopment area after approval;
- Reports on contracts made incident to the implementation and furtherance of a redevelopment plan or project;
- Cost of any property acquired, disposed of, rehabilitated, reconstructed, repaired or remodeled; and
- Number of parcels acquired through eminent domain proceedings.

Copies of all 37 redevelopment plans are not in the annual report although the state statute requires the annual report to include a copy of any redevelopment plan.<sup>7</sup> The redevelopment reports are bulky and it may be impractical to attach them to the annual report. Although these plans are not included in each annual report, TIF Commission staff send copies of plans and amended plans to the Missouri Department of Economic Development. Staff at the Missouri Department of Economic Development maintain files that include each redevelopment plan.

Although including each redevelopment plan in the annual report is not practical, the annual report should explain how readers could obtain a copy of a redevelopment plan. We recommend that the executive director of the TIF Commission include this information in future annual reports.

**Developers provided additional information in the annual report.**

The annual report also includes information provided by developers for most of the TIF plans. The TIF Commission surveyed developers to collect the information. It includes reported totals of project improvement investment, payroll within the districts, and expenditures related to removal of blight. Staff did not verify the information, and it was not provided for all 37 TIF plans.

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<sup>7</sup> RSMo 99.865 (10) requires, “the report shall include...a copy of any redevelopment plan, which shall include the required findings and cost-benefit analysis...”

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## **Finance Department Should Report Annually on Development Incentives**

The Finance Department should issue an annual report of financial information about TIF and other economic development incentives to the City Plan Commission and City Council. Such a report would enable the City Council, city management, and citizens of Kansas City to examine the use of incentives in the broader context of their impact on the city's overall fiscal condition by offering aggregate data on revenues, expenditures, debt levels, and associated portions of the tax base. The report would offer policymakers greater insight into the fiscal implications of incentive use and would serve as a reference when new TIF projects are being evaluated.

### **Aggregate Data Helps Evaluate the City's Financial Condition and Use of Development Incentives**

The City Council and city management need aggregate information on economic development incentives to better understand the city's overall financial condition and to evaluate the use of development incentives. Development incentives reflect significant city revenues and expenditures, represent a sizable percentage of the city's debt, and cover a significant portion of the city's property base. Because incentives are a significant financial activity, they should be related to the overall financial condition of the city.

#### **What do we mean by “aggregate” measures?**

Aggregates are totals of other measures. They provide overall information rather than specific details. For example, total assessed property valuation of all TIF sites is an aggregate measure. It is the total of the assessed value in each of the 37 TIF plans.

Members of the City Council have expressed interest in financial information and, in particular, in aggregate measures. The council's Finance and Audit Committee directed the city auditor to review the TIF annual report. Additionally, in reviewing aggregate financial information on the city's debt capacity, committee members have asked for information about the relationship between development incentives and debt capacity.

The Finance Department has expressed interest in collecting aggregate information about TIF and other development incentives. Although staff have begun to collect some aggregate information, the department has

not prepared a report to the City Council on aggregate measures related to development incentives.

Aggregate measures help policymakers evaluate incentive use on more than the singular merits of individual proposals. Like major capital expenditures, development incentives should be considered in the context of the city's overall financial condition. For example, in considering a specific TIF proposal, the City Council may want to view it in the context of the entire TIF program.

### **Measures Should Address Financial Condition**

The Finance Department should report aggregate measures to relate development incentives to the city's overall financial condition. Aggregate measures should address revenues and expenditures, debt levels, and tax base. The Finance Department, which is responsible for maintaining financial records and administering the financial affairs of the city, should report the measures to the City Council and the City Plan Commission.

**Revenues and expenditures.** The city's capacity to provide and manage incentive programs is directly related to revenues and expenditures. Financial management of any city program requires that policymakers understand the total revenues and expenditures associated with that program. This information is especially important for programs such as TIF, which encompass millions of tax dollars each year. Measures of TIF revenues and expenditures that should be reported yearly include:

- Total economic activity taxes and payments in lieu of taxes generated by TIF sites;
- Total TIF reimbursements for the year; and
- Comparisons of the growth in TIF and non-TIF revenues and expenditures.

**Debt levels.** While the risk associated with incentive-related bonds is typically less than with general obligation bonds, credit rating agencies consider incentive-related bonds when calculating the city's debt capacity and credit rating. The issuance of incentive-related bonds could diminish the city's ability to issue debt for other purposes without downgrading the city's credit rating. To account for this concern, city policymakers should have debt information including:

- Total amount of TIF bonds issued each year;
- Comparison of the amount of TIF bonds vs. other types of bonds issued each year;
- Total amount of outstanding TIF bonds;
- Percentage of the city's current and projected debt portfolio represented by TIF; and
- Percentage of the city's debt capacity represented by TIF.

**Portion of tax base.** By granting TIF to a parcel of land, the city foregoes its ability to generate full tax revenues on that piece of its tax base for up to 23 years. As the number of parcels that receive incentives grows, the city may find it increasingly difficult to generate future revenue growth. Alternatively, sites not included in TIF may be required to shoulder a higher burden for generating city revenues. Tax base measures that should be part of an annual report of aggregate TIF financial data include:

- Total assessed property valuations of all TIF sites;
- Percentage of the city's total assessed property value represented by TIF sites;
- Total amount of property (measured in either acreage or parcels) represented by TIF; and
- Percentage of the property within the city limits represented by TIF sites.

These types of aggregate financial information are also important tools for clarifying potential policy concerns underlying the need for incentives. For instance, if it is shown that a substantial percentage of the city's property receives incentives, policymakers can then question whether incentives are being overused or whether the use of incentives signals a poor business climate for attracting privately funded development to the city.

**The Finance Department should provide aggregate data on incentives.** Finance is responsible for maintaining financial records necessary to compile the data and for administering the financial affairs of the city. Furthermore, the department has the capacity to issue aggregate reports not only on TIF, but also on other economic development incentives such as Chapter 353 tax abatement and Chapter 100 bonds.

The Finance Department's report should supplement the TIF Commission's efforts to measure the performance of TIF. While the aggregate financial information is important, it does not answer questions

about whether an incentive program is performing up to expectations or providing a net benefit to the city. As we recommended in our 1998 performance audit, the executive director of the TIF Commission should develop performance measures for each plan to allow for an evaluation of the extent to which plans have addressed public goals. The TIF Commission should continue to develop performance measures for TIF projects and the TIF program as a whole.

### **Aggregate Data Should Be Reported to the CPC and Council**

According to the January 2000, economic development reorganization plan,<sup>8</sup> the City Plan Commission and City Council will serve as the two public bodies that review all projects seeking economic development incentives regardless of which incentive is being requested. As such, the Finance Department should consider those two bodies as the primary audiences for an annual report on incentive-related aggregate data and should be required to present their report to those entities by specified dates each year.

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## **Recommendations**

1. The executive director of the TIF Commission should include information in the annual report that describes how a reader can obtain copies of redevelopment plans.
2. The city manager should prepare for City Council consideration an ordinance that requires the Finance Department to provide the City Plan Commission and the City Council with an annual report on aggregate financial information related to economic development incentives and their impact on the city's fiscal capacity and condition.

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<sup>8</sup> Memorandum from Mayor Barnes, "Mayor's Reorganization of Economic Development", January 2000.



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## **Appendix A**

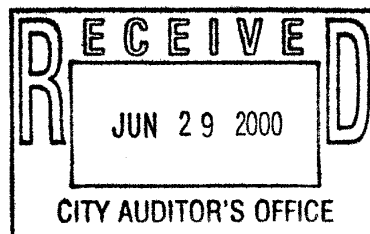
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### **City Manager's Response**





## Office of the City Manager



**DATE:** June 28, 2000  
**TO:** Mark Funkhouser, City Auditor  
**FROM:** Robert L. Collins, City Manager  
**SUBJECT:** Performance Audit – The 1999 TIF Annual Report

In response to your memorandum of June 12, 2000, City staff has reviewed the above referenced audit.

### ***Recommendations***

- 1. The City Manager should prepare for City Council consideration an ordinance that requires the Finance Department to provide the City Plan Commission and the City Council with an annual report on aggregate financial information related to economic development incentives and their impact on the City's fiscal capacity and condition.***

**Agree.** The audit recommends aggregate measurements relating to the City's revenues, expenditures, debt levels and tax base. The Finance Department along with the City Planning and Development Department and the Office of Management and Budget will work cooperatively to prepare this report.

Robert L. Collins

RLC:emm

cc: Wanda Gunter, Finance Department  
 Robert Langenkamp, City Planning and Development  
 Larry Plaisted, Management & Budget



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## **Appendix B**

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### **Executive Director of the TIF Commission's Response**

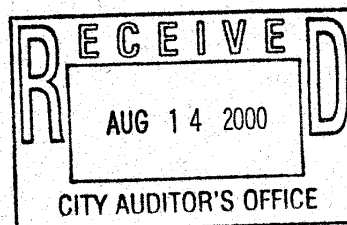




**TAX INCREMENT FINANCING COMMISSION OF KANSAS CITY, MISSOURI**

July 19, 2000

Mark Funkhouser  
City Auditor  
City of Kansas City, Missouri  
414 East 12<sup>th</sup> Street, 21<sup>st</sup> Floor  
Kansas City, MO 64106



RE: Response to Performance Audit – 1999 TIF Annual Report

Dear Mr. Funkhouser:

I would like to thank you for your comments and I am writing per your request for response to the Performance Audit of the 1999 TIF Annual Report as assigned by the Finance and Audit Committee on March 8, 2000.

***City Auditor's Recommendation***

*The executive director of the TIF Commission should include information in the annual report that describes how a reader can obtain copies of redevelopment plans.*

**Agree.** Detailed in the next annual report will be the address and phone number of our office in the event the reader would care to obtain a copy of a TIF plan or further information contained in the report.

I continue to support the forging of relationships between the City Manager, the various city departments and TIF Commission staff. Moreover, I appreciate your comments and request for comments. If you have additional questions or concerns, please contact me at 221-0636.

Sincerely,

John Crawford  
Executive Director  
Tax Increment Financing Commission

cc: Peter Yelorda  
Herb Kohn

**ECONOMIC DEVELOPMENT CORPORATION OF KANSAS CITY, MISSOURI**

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